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WASHBURN MILL CO. *v.* FIRE ASSOCIATION OF PHILADELPHIA.[1]
SUPREME COURT OF MINNESOTA. JANUARY 17, 1895.

Property was insured for the benefit of the mortgagee, as its interest may appear. Previous to such insurance the mortgage was duly foreclosed, the premium was paid by the mortgagee, but the time for redemption did not arrive until after the insurance.

It was *held* by the court that "the non-redemption from the mortgage sale by the owner of the premises did not work an alienation of the property, so as to defeat the policy, but that an action might be maintained in case of loss without notice to the insurance company of such non-redemption, and a notation thereof made on the policy, notwithstanding the policy provided that the mortgagee should notify the company of any change of ownership in the property insured, and that it be so noted on the policy."

EFFECT OF A MORTGAGE CLAUSE IN CONTRACTS OF INSURANCE.

From an early period in the business of insurance, resort has been had in various forms to these contracts as security for all kinds of indebtedness. To effect this class of security it has long been a custom with insurance companies and those dealing with them for the purpose of making their destructible property more valuable and desirable as security, to have a proviso embodied in the policy to this or like effect: "Loss, if any, payable to Richard Roe as his interest—or mortgage interest, as it is sometimes expressed—may appear." This seems to have been the earliest and is yet, perhaps, the most general mode of making a policy payable to one other than the assured for the purpose of security. Sometimes, too, the policy is assigned as collateral security for the same purpose.

[1] Reported in 61 Northwestern, 828.

There are some authorities which hold that where the assured obtains a policy and assigns it absolutely to another, the company consenting, this will operate as a new contract between the company and the assignee; that the assignor thereby becomes a stranger to the contract, and could neither receipt for the policy, prevent a recovery by the assignee, nor do any act which would invalidate the policy as to the assignee: *Pollard* v. *Insurance Co.*, 42 Me. 226. And in such cases, the action cannot be maintained, as a general rule, in the name of the assignee, but must be brought in the name of the assignor for the use of the assignee: *Flannagin* v. *Ins. Co.*, 1 Dutch. (N. J.) 506; *Folsom* v. *Ins. Co.*, 10 Foster, (N. H.) 231; *Pollard* v. *Ins. Co.*, *supra; Connover* v. *Ins Co.*, 3 Den. 254; *Coates* v. *Ius. Co.*, 58 Md. 172. And some of the authorities hold where the owner of the property insured has ceased to have any vested or contingent interest in the insurance, and the policy, by its terms, is made payable to the bearer or to a third person, or is so made payable after its execution by proper indorsement, such third party, bearer or indorsee may bring an action on the contract in his own name, as effectively as though the policy had been originally executed to such third party: *Barrett et al.* v. *Ins. Co.*, 7 Cuch. (Mass.) 175; *Hand* v. *Ins. Co.*, 57 N. Y. 41; *Motley* v. *Ins. Co.*, 29 Me. 337; *Cone* v. *Ins. Co.* 60 N. Y. 619.

In an early case in New York it was held that where insurance is granted to the owner of the property and payable in whole or in part to a third person, the action must be brought in the name of the originally insured unless he had transferred and conveyed the whole property to such third person, and that such party could not otherwise sue. This ruling was under a statute of New York, however, which provided "That, in case any one insured should sell and assign the subject of insurance, with the consent of the company before the loss, such vendee or assignee might bring an action on the policy in his own name. And when bringing the suit such assignee must not only show that he has an interest in the subject matter but that he has the whole interest." Otherwise he cannot sue—at least, alone: *Conover* v. *Ins. Co.*, 3 Den. 254.

In another case, in the same State, it was held in an action on a policy payable to a third person, as his interest might appear, that such language imports ownership in such person in the property insured, and that he or his assignee might maintain an action in his own name without joining the assured: *Pitney* v. *Glenns Falls Ins. Co.*, 65 N. Y. 6. But such words certainly do not import ownership. The interest may be partial and still be an interest. In another case it was held, that though the incumbrancer, to whom the insurance is made payable, may have realized from other securities the whole or a part of his mortgage debt, this will not prevent the incumbrancer from suing on a policy in his own name, nor will the company in such case succeed or be subrogated to the rights of the third party to whom the insurance is made payable. And the company cannot demand or make any inquiry as to the status of the accounts as between the third party and the owner of the property: *Cone* v. *Ins. Co.*, 60 N. Y. 619.

In an Iowa case where a policy was indorsed, payable to mortgagees as their interest may appear, it was held that the mortgagees could maintain an action on the policy, there being no other mortgagees, and this though the mortgage debt was satisfied before the action was brought, the consideration for the satisfaction of the mortgage, however, being a transfer of the property remaining after the fire, and the assignment of the policy: *Bartlett v. Iowa State Ins. Co.*, 77 Iowa, 86; 41 N. W. 579. But where the property thus undestroyed is transferred for a valuable consideration, with the policy of insurance, the assignee succeeds to all the rights of the assured and a settlement with the assignee for the liability incurred by issuing the policy would be wholly extinguished by making payment or satisfaction to the assignee. There is then no contingency whereby the assured could claim any right of action against the company. His assignment of the policy and transfer of the property covered thereby in payment of the mortgage debt completely extinguishes all his right and interest in the policy. It is held with very good reason in New Hampshire that where the mortgagee, for his protection, takes out a policy payable to himself as his mortgage interest may

appear, and his mortgage debt at the time of the loss is greater than the face of the policy, it is not necessary to make the nominally assured a party: *Hadley* v. *Ins. Co.*, 55 N. H. 110; *Chamberlain* v. *Ins. Co.*, 55 N. H. 249. This is reasonable. The interest insured here is not that of the mortgagor. It is taken out and paid for by the mortgagee for his own use and benefit and on property in which, by reason of his mortgage, he has an insurable interest. The mortgagor has no interest, whatever in a policy so issued, and the mortgagee having the sole and exclusive ownership and interest therein, it could serve no purpose to join the mortgagor as a party to an action on the policy. It seems to have been the rule in this State, in comparatively early times, when most of the insurance business was transacted through mutual companies, that the assured, by becoming a member of such company for the purpose of obtaining his insurance (his loss being directed by the terms of the policy to be paid to a designated person), the action must be brought by the assured, and cannot be maintained by such third party alone: *Nevins* v. *Ins. Co.*, 25 N. H. 22; *Rollins* v. *Ins. Co.*, 25 N. H. 200; *Folsom* v. *Ins. Co.*, 30 N. H. 231; *Blanchard* v. *Ins. Co.*, 33 N. H. 9; *Pierce* v. *Ins. Co.*, 50 N. H. 297. And in Illinois a comparatively early case announces the doctrine that where a policy is assigned by the insured, with the consent of the company, the assignee may sue on the policy for his own use in the name of the assured, but he cannot alone maintain the action. In this case, too, the policy was issued directly to the mortgagee, was for his exclusive benefit, and it was his interest only that was protected. A similar doctrine was laid down in Maryland where a policy was taken out on property which, at the time, was expressly made payable to the mortgagee by its terms, and which insured only the interest of such mortgagee. It was held that the policy, which by its terms insured one party but made the loss payable to another, would be construed in law as having been at its inception assigned to such third party with the consent of the company, and he is entitled to its benefits without procuring a transfer from the assured to the mortgagee with the consent of the company. Nor will the

fact that the mortgagor disposes of all his interest in the insured property prior to the bringing of the action by the mortgagee prevent the mortgagee from maintaining the action: *National Fire Ins. Co.* v. *Crane*, 16 Md. 260. In *Hammel* v. *The Queens Ins. Co.*, 50 Wis. 240; 6 N. W. 805, it is held that where a policy is made payable to the mortgagee as his interest shall appear, and if the debt due from the mortgagor exceed the face of the policy the legal title to the policy is in the mortgagee, and he can maintain an action thereon alone. This ruling was made by a divided court, ORTON, J., in a vigorous dissenting opinion stoutly maintaining that the mortgagor was a necessary party. The doctrine of this case finds support in *Travellers Ins. Co.* v. *California Ins. Co.*, 1 N. D. 151; 45 N. W. 703; *West Coast Lumber Co.* v. *Ins. Co.*, 98 Cal. 502; 33 Pac. 258. Ordinarily, however, where the insurance is issued on the application of the insured, and made payable to a third person by indorsement for the purpose of securing a debt, it is absolutely necessary that all who have an interest in the policy, vested or contingent, be made parties, either plaintiff or defendant, to the end that all rights thereunder may be adjudicated in one action, and that the company may not be unnecessarily harassed by two suits on a single contract. Let us suppose that A owes B \$500. A takes out a policy of insurance on his property for \$1000. For the better protection of his creditor, he has an indorsement placed on it making the loss, if any, payable to B as his mortgage interest may appear. The interest of B is clearly only five hundred dollars. A, too, has an actual interest in the same policy. A loss occurs, however, and B brings the action alone and in his own name. We will suppose that the whole of his debt is unpaid. Now, what is the effect of a recovery by B alone on this policy to the extent of his \$500? What is the effect if the insurance company is compelled to pay such a judgment? What would be the further effect if A should, after the recovery of the judgment and money by B, pay B off, which in duty he is bound to, do. B then has no interest in the policy, though he has recovered his \$500. He may be held a trustee, for A, perhaps, but what if he

squanders the money? A is not responsible to the company for B's conduct. He has the right to pay B at any time, and the very instant he does so, his right of action becomes entire and indivisible, and he has a just right to proceed against the company for the full face of his policy if he has complied with all its terms which he may, and is presumed, to have done. Of course the result might be the same if A owed B $1500 instead of only $500, according to some of the cases—only a very few, however,—if the face of the policy does not exceed the amount of the debt, the mortgagee may sue alone. Of course he can recover the whole amount of his debt when the amount of the policy is less than his debt, just as well as he could recover half of it if the face of the policy were double the debt. When the mortgage debt is paid, that, *ipso facto*, extinguishes every right of the mortgagee in the policy, he can thereafter bring no action on it, but the assured can bring it alone just as though there had never been any mortgage indorsement contained in the policy. Again, let us suppose that A takes out a policy on his house for $1000. He also borrows $1000 from B, and in order to secure B, he has the policy made payable to B as his mortgage interest may appear. A now really has his insurance money to start with. He may be little concerned in keeping the terms of the policy. If his house burns, he is not at any loss, for he knows B can sue on the policy and recover the full $1000. Suppose A then destroys his own house? If B can maintain the action, as some of the cases hold, the law will have permitted A to profit by his own infamy, and will allow B to recover on a policy issued to A, and insuring his property after A, according to the very terms of the contract under which B claims, and through whom he must receive any right to recover at all, has forfeited all right of recovery whatever. These illustrations have been resorted to show the dangers to which the rulings of some of the courts might lead, and the manifest injustice that might follow. And they further demonstrate the importance of the rule which permits the assignee or mortgagee to recover only when the assured or mortgagor himself could do so; and

that all who have an interest in the subject matter of the action should be made parties, to the end that all rights, arising under a single contract, might be adjudicated in a single action.

That an action on a policy where it is payable to a third person as mortgagee cannot be split up into two actions, and the company thereby subjected to two suits on one policy, is fortified not only by the better reasoning, but by most respectable authority as well: *Carberry* v. *Ins. Co.*, 86 Wis. 323, 56 N. W. 920; *Hartford Ins. Co.* v. *Davenport*, 37 Mich. 613; *Shove* v. *Shove*, 69 Wis. 425; 34 N, W. 392; *Thatch* v. *Ins. Co.*, 11 Fed. 29. See, also, *Norwich Union Ins. Soc.* v. *Standard Oil Co.*, 59 Fed. 984.

It is held in Illinois that when the insurance is effected by the mortgagor he holds the legal title, and may maintain an action on the policy for the use of the mortgagee: *Ill. Fire Ins. Co.* v. *Stanton*, 57 Ill. 354. This is especially true at common law under which the assignee of any chose in action cannot sue to enforce the rights assigned, in his own name, but must bring the action in the name of his assignor. This rule applies to that class of cases in which the policies are made payable in whole or in part to third persons, either by the terms of the policy itself, or by the assignment of the interest of the originally insured to another: *New England Fire & Marine Ins. Co.* v. *Wetmore*, 32 Ill. 221; *Flannigan* v. *Ins. Co.*, 1 Dutch. (N. J.) 506; *Folsom* v. *Ins. Co.*, 10 Foster, (N. H.), 251; *Pollard* v. *Ins. Co.*, 42 Me. 221; *Conover* v. *Ins. Co.*, 3 Den. 254; *Jessel* v. *Ins. Co.*, 3 Hill, 88; *Bowditch* v. *Ins. Co.*, 3 Gray (Mass.) 415; *Coates* v. *Ins. Co.*, 58 Md. 172.

It was held in *Wynne* v. *Niagra Fire Ins. Co.*, 91 N. Y. 185, that where a policy is payable to a third person as interest may appear, the owner of the property and mortgagee may well be joined as parties plaintiff in an action under the policy; that such mortgagee and insured have no adverse interest in the subject matter of an action, but, on the contrary, have a common interest in enforcing the contract; that the fund realized is applicable first, to the payment of the mortgage debt, and, if any remain, to the assured. To the same effect is the case of *Baynton* v. *Ins. Co.*, 16 Barb. 224, where it is further held that

where the assured, after assigning his policy as collateral, violates some of the provisions of the policy, there can be no recovery beyond the debt so secured, through both motgagee and assured are proper parties plaintiff.

Upon the issuance of a policy of insurance, loss, if any, payable to the mortgagee, as his interest may appear, some of the courts hold that the legal title is vested in the mortgagee by the terms of the mortgage itself: *Hammell* v. *Queens Ins. Co.*, 50 Wis. 240; 6 N. W. 805; *Travellers Ins. Co.* v. *California Ins. Co.*, 1 N. D. 151; 45 N. W. 703; *The Appleton Iron Co.* v. *Assur. Co.*, 46 Wis. 23; 1 N. W. 9. This being the case, the mortgagee could at least sue in his own name for the amount due him from the mortgagor, and could control any judgment that might be recovered to the extent of his interest. But while it may be conceded, for the sake of argument, that such a stipulation in a policy has this effect, yet the fact remains that this is only a contingent assignment of such legal title, and, upon the payment by the mortgagor to the mortgagee of the full debt thus secured, the title of the former in the policy revives and becomes paramount and exclusive. The clause does not effect an assignment of the policy either in whole or in part: *Martin* v. *Ins. Co.*, 9 Vr. 140; *Loring* v. *Ins. Co.*, 8 Gray (Mass.), 28. The contract of insurance is with the owner; it is to protect his property and not that of his mortgagee, and a loss under such policy is a loss to the assured, notwithstanding the mortgage clause, though the mortgagee has certain rights which the courts will protect: *Franklin Savings Institution* v. *Ins. Co.*, 119 Mass. 240; *Fogg* v. *Ins. Co.*, 10 Cush. (Mass.), 337; *Hale* v. *Ins. Co.*, 6 Gray (Mass.), 169. And the mortgagor will not be permitted to settle with the company and thereby exclude the rights of the mortgagee. His interest in the policy can still be enforced, though the assured may execute for a full consideration, a complete acquittance to the company: *Hathaway* v. *Ins. Co.*, 134 N. Y. 439; 32 N. E. 40.

In a case where the owner of property, upon which he had obtained a policy of insurance, subsequently mortgaged the same to secure a debt, and assigned the policy as collateral to

further secure the same, and upon the property being destroyed, the mortgagor instituted an action on the policy for the use of the assignee of the policy, the question arose in the case as to what effect a violation of any of the terms of the policy by the assured would have on the right of the mortgagee and assignee to recover. The opinion in the case shows great research and learning and is supported by the most unanswerable reasoning. The court reviews a number of cases on the subject and pays especial attention to that of *Traders' Ins. Co.* v. *Robert*, 17 Wend. 631, as well as other cases of the same tenor. The ruling of the lower court presented this question: "whether, where a policy of insurance has been assigned by the insured to one holding a mortgage on the premises, with the consent of the company indorsed upon the policy, its validity can be destroyed by acts done by the assignor in violation of its conditions." The court further says: "This question has received much discussion in the courts of New York and the decisions first made have been deliberately overruled. It was first held in *Traders' Ins. Co.* v. *Robert*, 9 Wend. 404, that no act of the assured, after the assignment of the policy, with the consent of the company, can impair the rights of the assignee. This case was approved and followed in *Tillou* v. *Ins. Co.*, 1 Seld. 406, the court holding that the assignment of the policy, with the assent of the insurer, creates new and mutual relations and rights between the assignee and the insurer, which cannot be impaired by a third person over whom the assignee had no control. The question again came up in *Grosvenor* v. *Ins. Co.*, 17 N. Y. 392, and in *Buffalo Steam Engine Works* v. *Ins. Co.*, Id. 401. In the first case the policy was not assigned by the mortgagor to the mortgagee, but by its original terms the loss, in case of fire was made payable to the mortgagee. The majority of the court held the cause was not distinguished from an assignment of the policy, and, overruling the cases already cited, held the policy was avoided by certain acts done by the mortgagor in violation of the terms of the policy. . . . In these two cases the question involved received a much fuller discussion than was given to it when the former decisions were rendered. In reply to the argument of the court in 9 Wend.

that the assignor could not be permitted to execute a release to the insurance company which would impair the rights of the assignee, and that he should not be permitted to do indirectly what he could not do directly, the court very justly says: 'This argument fails to distinguish between acts done for the purpose of discharging a liability and acts which, by the terms of the contract were necessary to be done or omitted in order to continue the liability of the company in force.'"

The Robert case also received a stunning blow at the hands of the Supreme Court of Pennsylvania in *State Mutual Fire Ins. Co.* v. *Roberts*, 31 Pa. 438, wherein STRONG, J., delivering the opinion of the court, among other things, said: "I am aware that there are to be found in the decisions of two courts of our sister States, adjudications that such assignments—assignments of the policy with the consent of the company—are equivalent to new policies issued to the assignees. Of course it is meant to refer to those cases where the assignee has an insurable interest, for, as the contract is one of indemnity, where there is no interest there can be no loss. The cases are. *Traders Ins. Co.* v. *Robert*, 9 Wend. 404; *Tillou* v. *Ins. Co.*, 1 Seld. 405, and *Charleston Ins. Co.* v. *Neve*, 2 McMul. (S. C.) 237. Both the latter were decided on the authority of the former. That was an action in the Supreme Court of New York, and so far as it relates to the doctrine now under discussion, has never been reviewed in the Court of Appeals. There a mortgagor, having effected an insurance on the mortgaged property, assigned his policy to the mortgagee with the assent of the insurers. It contained a condition against other insurance similar to that. After the assignment he effected other insurance upon the same property. It was held that though the assignee was compelled to sue in the name of the originally insured, yet the subsequent insurance did not affect his right to recover. He was treated as if the policy had been issued to protect his interest as mortgagee. It must be admitted that this case is in entire accordance with the ruling of the lower court in the case now before us. It was followed in New York by *Tillou* v. *Ins. Co.*, 1 Seld. 405, which was decided on its authority alone without any examination of the

correctness of the principle asserted in it. The South Carolina case was also decided with the Robert case in view, and in part rests upon it." The court then proceeds to note that these cases are exploded by the case of *Grosvenor* v. *Ins. Co.*, 17 N. Y. 391, and fully approves the reasoning of the court in that case. That this doctrine is correct and that the assignee of the policy succeeds to only the rights which the assignor might assign, finds support in *Carpenter* v. *Ins. Co.*, 16 Pet. 405, and *Weed* v. *Ins. Co.*, 116 N. Y. 120; 22 N. E. 229. In the latter case the policy was taken out on property, alleged to belong to the estate of a deceased person, and was made payable to a mortgagee and creditor of the estate as his interest might appear. The policy contained a provision that if the ownership of the assured was other than the sole and unconditional ownership it should be void. It turned out that the estate insured did not own the property, and it was held that the mortgagee acquired no rights by the indorsement.

It is certainly true, ordinarily, that where insurance is effected and afterward the assured disposed of the insured property, assigns the same to his vendee, the vendee taking the absolute dominion and ownership over the property covered, and the company consenting to such sale and assignment of the property and the policy, that thereafter no act of the originally insured can effect or in any way impair any rights whatever obtained by the assignee and vendee by reason of such transfer and assignment of the policy and property insured. For, in such cases the assured loses all control over and right to, or title in, the protected property. He becomes to both the company and the assignee a stranger and a third party, and could no more destroy or impair the subsequently vested rights of the assignee by setting fire to the property, or otherwise violating any of the stipulations or conditions of the policy than any other stranger in interest under the policy. After such assignment and sale there is no duty resting on the originally insured to any one. His rights are gone and in no event could he recover on the policy in whole or in part. The assignee becomes absolutely and for all purposes substituted to all the rights of the insured, and the assured will have no

greater rights in either the policy or property covered than the assignee had before such sale and assignment. Thereafter, the assignee and not the assignor, will be held to a compliance with the terms of the policy. He could not destroy the property himself or violate any of its conditions, simply because he derives his rights through another party on whom was enjoined the duty of keeping sacred the terms of the contract. Any other rule would be in defiance of justice and would merit and receive unqualified condemnation.

On the other hand, the general rule as established by the great weight of authority and what seems to be much the better reason, is that where the insurance is taken by the mortgagor, and the policy stipulates that the loss, if any, shall be payable to a third person as his interest may appear, or that where the policy is assigned or transferred by the mortgagor as collateral security, any violation of the terms of the policy by the insured, though without the knowledge or consent of the mortgagee, will avoid the policy and defeat a recovery by the latter: *Gillet* v. *Ins. Co.*, 73 Wis. 203; 41 N. W. 78; *Ins. Co.* v. *Hullman*, 92 Ill. 145; *Grosvenor* v. *Ins. Co.*, 17 N. Y. 391; *Bidwell* v. *Ins. Co.*, 19 N. Y. 179; *Hale* v. *Ins. Co.*, 6 Gray (Mass.), 169; *Perry* v. *Ins. Co.*, 61 N. Y. 214; *Weed* v. *Ins. Co.*, 116 N. Y. 106; 22 N. E. 229; *Pupke* v. *Ins. Co.*, 17 Wis. 389; *State Mutual Ins. Co.* v. *Roberts*, 31 Pa. St. 438; *Minock* v. *Ins. Co.*, 90 Mich. 236; 51 N. W. 367; *Phœnix Ins. Co.* v. *Willis*, 70 Tex. 12; 6 S. W. 825; *Carberry Ins. Co.* (Wis.), 56 N. W. 920; *Baynton* v. *Ins. Co..*, 16 Barb. 24; *Ins. Co.* v. *Stanton*, 57 Ill. 354; *Ins. Co.* v. *Hauslien*, 60 Ill. 521; *Ins. Co.* v. *Fix*, 53 Ill. 151; *Ins. Co.* v. *Davenport*, 37 Mich. 609; *Van Buren* v. *Ins. Co.*, 28 Mich. 404; *Ins. Co.* v. *Huron Salt & Lumber Co.*, 31 Mich. 346.

Where the insurance is thus made payable to a third party it is nevertheless the interest of the insured that is protected. The contract is with the assured, and the company agrees to pay him, or any other person designated, to receive the face of the policy in whole or in part. But if the assured fails or neglects to furnish proofs of loss, brings or has the action brought within the time stipulated in the policy; if he increases

the hazard contrary to the terms of the policy, makes such false statements in the application or is guilty of any fraud or bad faith in procuring the insurance; fails to give notice of the destruction of the property; contracts for additional insurance when forbidden by the policy to do so, or in any manner fails to perform and keep inviolate the contract on his part required by the policy to be kept, he cannot recover; and, as his assignee succeeds only to such rights as the assured had, his rights must fall with those originally injured. This is reasonable. If the assignee could recover regardless of what the assured might do in violation of the contract, it is clear that the company would be required in a sense to insure against a double or at least an increased hazard, whereas by the terms of the policy the company only undertakes to insure against a certain defined hazard, and receives pay only for what is thus expressed. That the companies could not do a profitable business if they were subjected to such consequences is clear, and the natural result would be bankruptcy or insolvency, and their very existence would soon be a thing of the past unless they should increase their rate of premiums sufficiently to meet this extra and unintended risk. Again, how would they increase their tariff of premium rates? It would be inequitable to make those patrons who do not mortgage the insured property and assign the policy as collateral, or have it made payable to a mortgagee, to pay the same rate of insurance exacted for the greater hazard. And how are the companies to know when the policy holder will assign his chose in action? This is impossible and the underwriter's only safe course would be to charge every one a rate of premium which would be commensurate with the greater hazard. This is clearly wrong. And to illustrate the force of this contention we will suppose that A takes out a policy of insurance for $1000. The property, perhaps, is not worth more than this sum. He owes B $1000 and transfers the policy to him as collateral to secure it. He also owes C $1000 and executes to C a mortgage on the insured premises to secure this $1000 after the transaction with B. He makes default with C and the latter forecloses the mortgage and sells the property, completely divests A of

his title in the insured property, and makes his mortgage debt by the foreclosure. After the foreclosure and during the life of the policy, the property is destroyed by fire. B now resorts to his policy and compels the insurance company to pay his $1000. A has practically sold the property before the fire, yet he gets the full benefit of the insurance, and the obliging company is compelled to pay A's. debt to B for him. It might be answered to this that the company would be subrogated to B's right to collect his $1000 by being compelled in law to pay the same. But suppose the property insured is all that A had, or is exempt under the laws of the state in which he lives? Would this place the company in any better attitude? It may be that A destroyed the house himself after the mortgage foreclosure for the very purpose of requiring the company to pay his debt to B; and according to that line of cases which hold that no act of the originally insured can affect the rights of the assignee, or the party to whom the policy is made payable for the purpose of securing a debt. It is patent that a large per centum of such losses as this would be ruinous to any company. It would be impossible for it to do business in the face of such odds for any great length of time, and the eve of prophecy would behold in unerring certainity its early downfall and ruin. It is clear, therefore that the better reason as well as natural justice is with that line of decisions which hold that when a policy is taken out by the assured, and made payable to a third party, as his interest may appear, or is by the assured assigned, either absolutely or as collateral, such third party or mortgagee, assignee, or other party in interest, can only recover where the assured could have done so had the policy not been assigned or in any manner transferred.

It is true that this rule will not obtain, perhaps, where the mortgagee—who, of course, has an insurable interest in his mortgagor's property—should for his own protection, procure a policy of insurance on the mortgaged property. In this case, of course, the insurance contract is with the mortgagee. The mortgagor has no interest therein whatever. Neither his property nor any interest of his is covered by the policy. He

did not apply for the insurance, did not pay the premium and no policy was issued or made payable to him, and no act of his—not even the willful destruction of his property by him—could preclude the right of recovery in the mortgagee. In cases of this kind there is nothing to revert to the mortgagor. He may pay his debt, and this will only have the effect of practically cancelling the insurance, for the mortgagee has an insurable interest in the property by reason of his debt secured by his mortgage. When that is satisfied, he has nothing to insure, and he can suffer no loss by the destruction of the property. Not so, however, where the policy is issued to the mortgagor and made payable to the mortgagee as his mortgage interest may appear. When this is the case it is plain that the payment of the secured debt would have the effect of vesting the full right to all the insurance in the mortgagor, for, the interest of the mortgagee being extinguished, his right in the policy ceases as it was only contingent on the existence of his debt. When that was extinguished the mortgage interest in the policy and the property covered *ipso facto* ceased and became extinguished. The insured thereby becomes entitled to recover on the policy just as though there had been no mortgage transaction whatever. In harmony with this rule it is held by many courts of the highest respectability that the effect of the clause making the policy payable to a third party as mortgagee, etc., is but a direction in advance of any loss to pay the money, when due, to a designated party; which payment, when so made by the company, discharges its liability to the extent of the interest of such third person in the policy, the assured, of course, being entitled to anything that may remain: *Martin* v. *Franklin Ins. Co.*, 9 Vr. 140; *Turner* v. *Ins. Co.*, 109 Mass. 573; *Fogg* v. *Ins. Co.*, 10 Cush. (Mass.) 346; *Loring* v. *Ins. Co.*, 8 Gray (Mass.) 29; *Hale* v. *Ins. Co.*, 6 Gray (Mass.) 169; *Franklin Savings Institution* v. *Ins. Co.*, 119 Mass. 240.

There has come into use, of late years, however, a mortgage clause very different from any that has been considered. It seems designed to avoid the consequences of some of the decisions under the simple mortgage clauses, on the one hand,

and to the better and more definitely set out the rights and liabilities of the parties, on the other. It is as follows: "Loss, if any, payable to A. B., mortgagee or trustee as hereinafter provided. It being hereby understood and agreed that this insurance, as to the interest of the mortgagee or trustee only herein, shall not be invalidated by any act or neglect of the mortgagor or owner of the property insured, nor by the occupation of the premises for purposes more hazardous than are permitted by the terms of this policy; provided, that in case the mortgagor or owner neglects or refuses to pay any premium due under this policy, then, on demand, the mortgagee or trustee shall pay the same; provided, also, that the mortgagee or trustee shall notify this company of any change of ownership or increase of hazard which shall come to his or their knowledge, and shall have permission for such change of ownership or increase of hazard duly indorsed on said policy; and, provided, further, that every increase of hazard not permitted by the policy to the mortgagor shall be paid for by the mortgagee or trustee on reasonable demand, and after demand made by this company, upon and refusal by the mortgagor or owner to pay according to the established schedule of rates. It is, however, understood that this company reserves the right to cancel this policy as stipulated in the printed conditions in said policy; and, also, to cancel this agreement on giving ten days' notice of their intention to the trustee or mortgagee named therein, and from and after the expiration of the said ten days this agreement shall be null and void. It is further agreed that in case of any other insurance upon the property hereby insured, then this company shall not be liable under this policy for a greater portion of any loss sustained than the sum hereby insured bears to the whole amount of insurance on said property issued to or held by any party or parties having an insurable interest therein. It is also agreed that whenever this company shall pay the mortgage or trustee any sum for loss under this policy, and shall claim that as to the mortgagor or owner no liability therefor exists it shall, at once, and to the extent of such payment, be legally subrogated to all the rights of the party to whom such payments shall be

made, under any and all securities held by such party for the payment of said debt. But such subrogation shall be in subordination to the claim of said party for the balance of the debt so secured. Or, said company may, at its option, pay said mortgagee or trustee the whole debt so secured with all the interest which may have accrued thereon to the date of such payment, and shall thereupon receive from the party to whom such payment shall be made an assignment and transfer of said debt, with all securities held by such parties for the payment thereof." The reports do not amount in decisions and precedents under these comprehensive mortgage clauses, but the few cases hold, iron-clad as these mortgage clauses are, that they do not dispense with the requirements of the policy except to the extent only that they are not required by the express provisions of the mortgage clause: *Hastings* v. *Ins. Co.*, 73 N. Y. 141; *American Building & Loan Association* v. *Farmers' Ins. Co.*, (Wash.) 40 Pac. 125. In the latter case, the court explaining the effect of such a mortgage clause, among other things, says: "All the provisions of the policy continued in force, excepting only such as are inconsistent with the provisions contained in the clause annexed; but general provisions of the policy intended for the security and protection of the company, and which do not relate personally to the mortgagor, such as the stipulation concerning the time in which the action shall be brought, are not abrogated or affected by it. Resort must still be had to the terms of the policy to ascertain many things which are the very life of the contract; among others, the amount of insurance, the property insured, the term of the insurance, and very many matters concerning which the indorsement itself furnishes absolutely no information whatever." This is all well said. For, suppose the term of the policy has lapsed or expired? A recovery could not be had thereafter on the policy simply, forsooth, because the mortgage clause had been attached. Likewise the stipulation that the action on the policy must be commenced within the period named in the policy notwithstanding such mortgage clause; *American Building & Loan Assn.* v. *Farmers' Ins. Co.*, *supra*. And where an action is

brought by the mortgagee on a policy containing such a stipulation, not even the wilful or wanton destruction of the property by the assured will defeat the right of the mortgagee to the extent of his mortgage interest, to recover; *Hartford Fire Insurance Co.* v. *Williams*, 63 Fed. 925. Such an act, it is true, is a fraud upon the company so far as the assured is concerned, and should he, after such destruction of the property by himself, pay off and extinguish the mortgage debt, the mortgagee's interest in the policy being thereby terminated and ended, no recovery could be had on the policy at all. All rights of the assured being defeated by his own act, the policy becomes absolutely of no force. But if the mortgagee should, before such payment of the debt to him by the assured, first collect the amount of his mortgage interest from the insurance company, the company, upon the payment of the mortgage debt by the assured to the mortgagee, would doubtless have its right of action against the mortgagee for such sums as it may have paid him under the mortgage clause.

While this mortgage clause stipulates that the policy, as to the interest of the mortgagee "shall not be invalidated by any act or neglect of the mortgagor or owner of the property insured, etc.," this clause must nevertheless yield to another clause in the policy which provides that the insurer "shall not be liable under this policy for a greater portion of any loss than the sum thereby insured bears to the whole amount of insurance on said property, issued to or held by any party or parties having an insurable interest therein." In such case the mortgagee will be required to prorate the insurance covered, as it were, by his mortgage clause, with any other insurance which the mortgagor or any other person having an insurable interest in the insured property, who may have also taken out on the same property: *Hartford Fire Ins. Co.* v. *Williams*, *supra.*

Such a mortgage clause has the effect of making a separate contract of insurance with the mortgagee to the extent of the mortgage interest: *Westchester Fire Ins. Co.* v. *Coverdale*, 48 Kan. 446; 29 Pac. Rep. 682; *Phenix Ins. Co.* v. *Omaha Land & Trust Co.* (Neb.), 60 N. W. 133; *City Five Cent*

Savings Bank v. *Ins. Co.*, 122 Mass. 165; *Ins. Co.* v. *Olcott*, 87 Ill. 439. And the clause must be construed with all the provisions of the policy, and not alone when there is any doubt as to its effect: *Hartford Fire Ins. Co.* v. *Williams*, *supra*; *Meriden Savings Bank* v. *Ins. Co.*, 50 Conn. 396. And the clause does not partake of the nature of an assignment of the interest of the insured, in whole or in part, to the mortgagee: *Phenix Ins. Co.* v. *Omaha Land and Trust Co.*, *supra*, and in this case it is further held that the failure of the assured to give written notice of loss under the policy, as provided by its terms, will not defeat the right of the mortgagee to recover, and the mortgagee may maintain an action on the policy in his own name and alone for the amount of his mortgage debt, especially if no objection is made in the trial court to the want of proper parties: See also *Meriden Savings Bank* v. *Ins. Co.*, *supra*. But, on principle, whether it be necessary for the insured to give the written notice of loss or not, it would certainly be well for the mortgagee to do so if in his power. And the mortgagee should, doubtless, use every effort to have the assured make the proofs of loss required by the policy, and, if it is in the power of the mortgagee to fulfil this requirment, he should, out of abundance of caution, if for no other reason, make the necessary proofs himself, though if it be out of his power to do so, and the assured refuses, the mortgagee could still, no doubt, recover by virtue of the mortgage clause. But the law certainly enjoins upon him the duty of exercising at least ordinary diligence and the utmost good faith.

These comprehensive and binding mortgage clauses seem to have been necessitated from a demand on the part of mortgagees for better security for their debts than the simple and short clause making the insurance payable to a third as his interest might appear, or an assignment of the policy as originally written as collateral security. In all their details they have not been passed upon by the courts, and it is noticeable that the decisions afford but little light except as to some portions of the clause which have received judicial consideration. These lengthy clauses are not all exactly alike, some

going much more into detail than others. It is apparent, however, that they all have in view one of the very controlling ideas that the insured cannot, by any act of his own, defeat a recovery by the mortgagee to the extent of his mortgage debt. Certain duties are also devolved upon the mortgagee, such as giving notice of increased hazard, change of occupation, etc., when the same may become known to him, and he is required to pay the necessary additional premium for any increased hazard according to the usual tariff of rates for such, and the company, upon certain notice, for its protection, reserves the right to cancel the policy even as to the mortgagee. Nor can the mortgagee recover for his debt simply by declaring on the policy as it is written with the mortgage clause. It must affirmatively appear that he has a valid debt secured, that it is unpaid, and what the amount is. In short, he must show his interest in the policy, else his complaint will be vulnerable to demurer: *Commercial Union Assur. Co.* v. *Dunbar* (Tex. Civ. App.), 26 S. W. 628.

Out of the somewhat confused and contradictory state of the decisions, it is fairly safe to lay down the following general rules as sustained by the better reason and authority:

1. Where the loss is simply made payable to the mortgagee as his interest may appear, it is but a stipulation for the payment of the mortgage debt to such third party, and the third party can recover nothing under the policy where the assured himself could not do so. The mortgagee can in no event succeed to a greater or paramount right than that possessed by him from whom he receives the right to collect for his mortgage debt, the insurance being taken out on the property, and at the instance of the assured and paid for by him.

2. Where the insurance is taken out by the mortgagee, for his own benefit, though the policy is written in the name of the nominally insured, and made payable to the mortgagee as his mortgage interest may appear, the mortgagee will be entitled to bring the action in his own name to the extent of his debt so long as any part thereof is in existence, and the assured can do nothing to defeat the terms and provisions of the policy.

3. Where the insurance is primarily taken by the assured and the policy contains the provision making it payable to a third party as his interest may appear, the action on the policy must be brought in the name of the insured for the use of the mortgagee, as a general rule, and if the face of the policy exceeds the amount of the debt secured, the action cannot be maintained by the mortgagee alone, but the assured must be joined as a party.

4. Where, instead of making the loss payable to the mortgagee by the terms of the policy, it is assigned to him as collateral security, the suit at common law must be brought in the name of the assignor, and the right of the assignee to recover will depend on the right of the assured to have recovered if there had been no assignment of the cause of action.

5. Where the policy contains the iron-clad mortgage clause, the mortgagee may sue in his own name for that part of the insurance which secures his mortgage debt, and no more.

6. The mortgagee, before he will be entitled to recover at all, must show a subsisting debt secured by the policy or the mortgage clause before he will be permitted to recover anything in any event. And he must do and perform in good faith all things on his part to be performed under the policy and the mortgage clause, which should be construed together, and he is bound by all the terms and conditions of the policy not in irreconcilable conflict with the mortgage clause.

7. No act of the assured, such as the wilful destruction of the insured property, or failure to comply with any of the condititions of the policy required to be performed by the insured, will defeat an action by the mortgagee on a policy containing the iron-clad clause.

W. C. RODGERS.

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